

* [NOTE: SPECIAL SURVEY EDITION](#) . *This week's edition includes an interactive survey. After you finish reading, please make sure to assess my plan and tell me what you think!*

Taxes: Taxes are always a big issue in politics and public policy. However, right now there is a crescendo of agreement building in Washington that it's time to make some fundamental change to our tax system.

The debate in Washington of late has been confined to the so-called Bush tax cuts, all of which are scheduled to expire at the end of this year. Essentially, should we extend all of them, none of them, or some of them? The erudite readers of these missives (that's you) have heard all of this before and know the arguments for and against the extension and all about taxing the "rich" and such. So, I won't repeat them here. Economists are unified in their predictions of recession if we are allowed to go over the "fiscal cliff" on December 31 and allow all of the tax cuts to expire and the sequestered spending cuts take effect. Those cries are not falling on deaf ears in Washington. I think that eventually all of the Bush tax cuts will be extended for somewhere between 6 months and one year. I don't know whether that vote will happen before or after the election, but I think the fragility of the economy necessitates this action and reasonable minds will prevail at some point.

But, no one is happy with the current tax system. And, no one is happy with the idea that there is no permanency to the tax code today and that so many elements of it expire every year. This adds a totally unnecessary uncertainty into the economy that hampers decision making and is one of the many factors restricting our growth. And frankly, lawmakers hate the fact that every year or so we are faced with the Hobson's choice of either raising taxes or allowing the deficit to rise. That is not a vote that any Republican or Democrat relishes taking. So, the 1 year or 6 month extension this year should be about giving us time to try to completely remake the tax code in 2013.

Many of you know that I am the only member of Congress with a Master's Degree in Business Taxation (MBT). I received that degree from USC (Fight on!) in 1977. I am a CPA and once prepared tax returns for a living. At that time, I learned the Internal Revenue Code of 1954. We now have the Internal Revenue Code of 1986. I believe we may soon see the Internal Revenue Code of 2013.

But, what will that code look like? We ought to "reach for the stars" here. Let's not just tinker with the tax code and change it a little bit. Let's see if we can get 218 votes in the House, 60 votes in the Senate and the signature of whoever is president on a complete restructuring of the Code that would make it flatter and simpler.

It's actually pretty clear what to do on the corporate tax side. Eliminate a bunch of deductions and credits and get the rate down from the current 35% to hopefully 25%. Of course, the trick is getting that done. Every corporation will favor a lower rate, but most will fight to keep their deductions in favor of cutting the others. In my opinion, deductions should follow accounting principles. If they are greater than what we allow on a financial statement, then it's some form of tax benefit. We may want to keep a few tax benefits for some industries (like manufacturing) to remain competitive in the world market, but most of them should go. And, we should allow US corporations to repatriate their overseas earnings without penalty.

The bigger issue, however, is what we do with individual taxes. Obviously, these are the taxes we all pay on our wages and investment income and such. But, the vast majority of businesses pay taxes under individual tax rates if they are formed as a "pass-through entity", like a partnership, LLC, subchapter S corporation or sole proprietorship. I have seen estimates that show roughly 1/3 of individual income taxes are actually paid on income from a business in one of those entities. So, that being said, the individual tax system is the one that will have the most impact upon economic growth simply because it affects absolutely everyone in one way or another.

Now, you have already read that I have a background in this area. Accordingly, this is not my first rodeo. For the last 6 years, Paul Ryan (R-WI), Jeb Hensarling (R-TX) and I have been the authors of a bill called the Optional Simplified Tax. It created a new, optional tax code with 2 tax rates and absolutely no deductions. It was optional (you could elect to continue to pay on the "old" system and rates) because we were unsure when we wrote it 6 years ago that the public was ready for this radical a change. I now think that the public has shifted some and is ready for radical reform. But, I have shifted some too.

Over the last 6 years, my thoughts on what a new, reformed tax system should be have changed. In fact, my thinking has changed in the last 6 weeks. The point in telling you this is to highlight that there is no obvious solution here, regardless of your particular political or economic philosophy. There are good arguments for and against different alternatives.

So, I'm going to present to you what, at this point in time, I would do with the individual tax system if I were king. And, I'm giving you the opportunity to vote right here on the major elements of it and tell me if you agree with me or not. I'll be interested to see what you all think. And, I'll also tell you in a future laptop how you all responded. Feel free to disagree with me. I may disagree with me after I think about it a little more.

So, here's my description of the **JC Tax Code of 2013, Version 2.0**:

- **Eliminate all deductions except: charitable contributions, home mortgage interest and non-elective medical expenses.** This will mean that we cannot get to a 25% income tax rate. It will have to be higher than that. I used to think that we should eliminate all deductions and take the lower rate and the added simplicity. But, I now have persuaded myself that it is important that individuals fund as many societal needs as possible through charitable activities rather than leaving them to inefficient and biased government allocation. Eliminating the charitable deduction would make that much more difficult. Medical expenses (other than cosmetic surgery and such) are a burden none of us want to spend money on. But if we have to, I think we should do it with pre-tax dollars - particularly when we return the control of medical care to the individual and take it away from the government by repealing Obamacare and replacing it with a system where we each have the freedom to make our own medical decisions. Finally, the home mortgage deduction has long been a staple of "The American Dream" of homeownership, and an integral part of our economy. If we eliminate it, homeownership will drop further, causing jobs and the economy to suffer mightily.

- **Go to 2 tax rates: one for incomes below \$100,000 (maybe 20% under this scenario) and a second for incomes above that (something like 28%).** I know that the single "flat tax" rate has a guttural appeal to many of you. But, there is no way to implement a truly flat tax (and keep the total revenue collected about the same) without raising taxes on the middle class and cutting them for higher incomes. I do not share Obama's desire to punish the "rich". But, neither do I think that raising middle class taxes in order to achieve a top rate below 25% is a good trade-off.

- **Allow corporations to deduct dividends from their income, but make dividend income taxable as ordinary income with no preferences to individuals.** This is complicated stuff. Dividends are currently taxed at a maximum of 15%, but the dividend payment is not deductible to the corporation that pays it out. I propose that we tax dividends like any other type of income at whatever the full rate winds up being, but allow corporations to deduct the dividend the same way they deduct interest payments on bonds. This will put debt and equity on an equal footing in corporate boardrooms as a method of raising cash. Which will mean more equity issuance and less debt. This is a good thing. And, we also eliminate the complexity of another "class" of income at the individual level.

- **Eliminate any preferences for capital gains, except for non-depreciable assets held over 5 years.** We have always defined capital gains as any gain from the sale of a "capital" asset. I propose that we change that. I propose that all gains on sales of anything held for less than 5 years are taxed at the same rate as any other income. I don't know why "trading" or other short-term income should get a lower rate than a salary or interest income. But, we do need a lower rate (maybe 10%) for sales of non-depreciable assets that have been held for 5 years or longer. There is a simple elegance to having all income, regardless of its character, taxed at the same rate - that would mean no preference for capital gains or anything else. I am romanced by such a prospect. But, the economic reality is that a high tax rate on the sale of long-term assets will discourage people from selling them and moving that asset to someone who will make better use of it, thereby creating jobs. So, I think a 10% rate on gains from the sale of non-depreciable assets held more than 5 years makes sense.

- **Implement a minimum tax so that anyone with any income at all pays 2% of their gross income or a minimum of \$100.** You have probably read that over 50% of Americans now pay no income tax at all. A few of these are relatively wealthy people with all their money in tax-free municipal bonds. But, most are lower income people or people with a lot of deductions. In fact, 50% of Americans pay nothing at all for national defense, national parks, or the court system, in spite of the fact that they undoubtedly benefit from all of these services and more. Everyone who earns a paycheck or a dividend payment should participate in the funding of the basic elements of American government. The top 20% of incomes will still fund 67.9% of everything. But, everyone with income will participate in some way. Society succeeds when all pay and all benefit. Society fails when a few pay and most receive.

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This is serious and complicated stuff. The humor in the survey is injected to make it readable and to try to take some of the mouth-destroying dryness out of tax accounting. But, your answers will be taken seriously and this debate is very important.

I will let you know what you all have to say. Maybe you'll change my mind.....

Until then, drive fast and live free....